Section 141.—Private Activity Bond; Qualified Bond

26 CFR 1.141–7: Special rules for output facilities.

T.D. 9016

DEPARTMENT OF THE TREASURY
Internal Revenue Service
26 CFR part 1

Obligations of States and Political Subdivisions

AGENCY: Internal Revenue Service (IRS), Treasury.

ACTION: Final regulations.

SUMMARY: This document contains final regulations on the definition of private activity bonds applicable to tax-exempt bonds issued by state and local governments for output facilities. These regulations affect issuers of tax-exempt bonds and provide needed guidance for applying the private activity bond restrictions to output facilities.

DATES: *Effective date:* These regulations are effective November 22, 2002.

Applicability date: For dates of applicability, see § 1.141–15 of these regulations.

FOR FURTHER INFORMATION CONTACT: Rose M. Weber (202) 622–3980 (not a toll-free number).

SUPPLEMENTARY INFORMATION:

Background

This document amends the Income Tax Regulations (26 CFR part 1) under section 141 by providing special rules for tax-exempt bonds issued for output facilities. On January 18, 2001, temporary regulations (T.D. 8941, 2001–1 C.B. 977) (the temporary regulations) were published in the **Federal Register** (66 FR 4661) to provide guidance under the Internal Revenue Code of 1986 regarding, among other things, (a) the application of the private activity bond tests under section 141(b)(1) and (2) to output contracts for output facilities; and (b) the application of the $15 million limit under section 141(b)(4) to output facility financings. A notice of proposed rulemaking (REG-114998–99, 2001–1 C.B. 992) cross-referencing the temporary regulations was published in the **Federal Register** on the same day (66 FR 4754). On July 24, 2001, the IRS held a public hearing on the proposed regulations. Written comments responding to the notice of proposed rulemaking were also received. After consideration of all the comments, the proposed regulations are adopted as amended by this Treasury decision and the temporary regulations are removed. The revisions are discussed below.

Explanation of Provisions

A. *§ 1.141–7 Special Rules for Output Facilities*

1. *Benefits and burdens test*

The temporary regulations contain a benefits and burdens test for determining whether the purchase of output of an output facility is taken into account under the private business tests. In particular, the temporary regulations provide that the purchase by a nongovernmental person of available output of an output facility is taken into account under the private business tests if it has the effect of transferring substantial benefits of owning the facility and substantial burdens of paying the debt service on bonds used to finance the facility. Under this test, an output contract transfers substantial benefits of owning a facility if it gives the purchaser (directly or indirectly) rights to capacity of the facility on a basis that is preferential to the rights of the general public. An output contract transfers substantial burdens of paying debt service under this test to the extent that the issuer reasonably expects that it is substantially certain that payments will be made under the terms of the contract (disregarding default, insolvency, or other similar circumstances).

Commentators were generally critical of the benefits and burdens test in the temporary regulations. Some commentators stated that preferential rights is not an adequate concept for determining whether substantial benefits of ownership are passed through an output contract. Some commentators suggested that a substantial certainty of payment by a purchaser does not necessarily constitute a transfer of substantial burdens of paying debt service. Other commentators recommended that any sale of output by a municipal utility outside of its traditional service territory should result in private business use.

The final regulations amend the benefits and burdens test. Under the revised provision, an output contract is taken into account under the private business tests if it has the effect of transferring to a nongovernmental person the benefits of owning the facility and the burdens of paying the debt service on bonds issued to finance the facility. This test is met if a nongovernmental person agrees to purchase available output of a facility pursuant to (1) a take contract (that is, a contract under which the purchaser agrees to pay for the output if the facility is capable of providing it), or (2) a take or pay contract (that is, a contract under which the purchaser agrees to pay for the output, whether or not the facility is capable of providing it). In addition, as discussed below, certain requirements contracts may satisfy the benefits and burdens test. The final regulations define *requirements contract* as an output contract, other than a take contract or a take or pay contract, under which a nongovernmental person agrees to purchase all or part of its output requirements.

2. *Requirements contracts*

The temporary regulations provide that a requirements contract under which a nongovernmental person agrees to purchase all or part of its output requirements is taken into account under the private business tests to the extent that, based on all the facts and circumstances, it meets the benefits and burdens test in those regulations. Relevant factors in making this determination include whether the purchaser's customer base has significant indicators of stability, whether the contract covers historical (rather than only projected) requirements, and whether the purchaser agrees not to construct or acquire other resources. A requirements contract that is not a sale at wholesale (a retail requirements contract) generally does not meet the benefits and burdens test in the temporary regulations, except to the extent it obligates the purchaser to have requirements or to make payments that are not contingent on its requirements. Reasonable and customary damages and termination provisions do not cause a requirements contract to meet the benefits and burdens test under the temporary regulations.

Most commentators were critical of the treatment of requirements contracts in the temporary regulations. Some commentators stated that the factors for analyzing requirements contracts are not administrable and do not necessarily indicate whether a purchaser has acquired substantial benefits of ownership or burdens of debt service. Other commentators requested that the regulations be amended to specify that requirements contracts with power marketers or with purchasers located outside the service territory of a municipal utility result in private business use.

The final regulations provide two rules under which a requirements contract may satisfy the benefits and burdens test. First, a requirements contract (retail or wholesale) generally meets the benefits and burdens test to the extent that it contains contractual terms that obligate the purchaser to make payments that are not contingent on the output requirements of the purchaser or that obligate the purchaser to have output requirements. Second, the final regulations continue to apply a facts and circumstances approach for wholesale requirements contracts, but provide simplified factors and two safe harbors. Under this approach, the following factors tend to establish that a wholesale requirements contract meets the benefits and burdens test: (1) the term of the contract is substantial relative to the term of the issue and (2) the amount of output to be purchased represents a substantial portion of the available output. A wholesale requirements contract does not meet the benefits and burdens test under the facts and circumstances approach if it satisfies one of the following safe harbors: (1) its term does not exceed the lesser of five years or 30 percent of the term of the issue or (2) the amount of output to be purchased does not exceed five percent of the available output of the facility.

3. *Pledged contracts*

Under the temporary regulations, payments under an output contract that is pledged as security for an issue are taken into account under the private business tests even if they are not substantially certain to be made. A contract is pledged for this purpose only if the bond documents prohibit substantial amendments of the contract without the consent of bondholders.

Some commentators suggested that this provision adds undue complexity and is unnecessary in light of the benefits and burdens test. The final regulations adopt this comment and delete the provision.

4. *Exception for small purchases of output*

The temporary regulations provide that an output contract is not taken into account under the private business tests if the average annual payments under the contract that are substantially certain to be made do not exceed 0.5 percent of the average annual debt service on all outstanding tax-exempt bonds issued to finance the facility, determined as of the effective date of the contract.

Some commentators recommended that the 0.5 percent threshold be increased to one percent, and that the exception refer to guaranteed minimum, rather than substantially certain, payments. Other commentators recommended that the exception be deleted. The final regulations increase the 0.5 percent threshold to one percent and specify that all payments to be made under the contract are taken into account.

5. *Exception for short-term sales of output*

The temporary regulations contain an exception under which an output contract with a nongovernmental person is not taken into account under the private business tests if: (1) the term of the contract, including all renewal options, does not exceed one year; (2) the compensation under the contract is based on generally applicable and uniformly applied rates or represents a negotiated, fair market price; and (3) the facility is not financed for a principal purpose of serving that nongovernmental person.

Most commentators recommended that this exception be expanded to permit contracts of a longer duration. These commentators stated that longer-term contracts are required in order to transfer benefits of ownership and burdens of debt service with respect to an output facility. Other commentators suggested that the exception should be narrower in scope. These commentators recommended that the exception take into account the entire anticipated period of ongoing sales, irrespective of the term of any contracts or renewal options.

The final regulations retain and amend the exception for short-term output sales. In order to exclude from the private business tests output contracts that do not transfer the benefits of ownership and the burdens of debt service, the final regulations increase the one-year period to three years.

6. *Exception for swapping and pooling arrangements*

The temporary regulations provide that certain agreements to swap or pool output do not result in private business use to the extent that: (1) the swapped output is reasonably expected to be approximately equal in value, determined over periods of one year or less; and (2) the agreement is entered into for a qualifying purpose, such as enhancing reliability.

Some commentators recommended that the exception be expanded to apply to transactions in which the value of the swapped output is not approximately equal, but the governmental person is a net importer of power. The final regulations do not adopt this recommendation because such transactions may not in substance constitute power swaps, and are more appropriately analyzed under the benefits and burdens test.

The final regulations retain the exception for swapping and pooling arrangements, but increase the one-year period to three years.

7. *Special rule for facilities with significant unutilized capacity*

The temporary regulations provide that, if an issuer reasonably expects on the issue date that persons that are treated as private business users will purchase more than 20 percent of the actual output of the facility, the Commissioner may determine the number of units produced or to be produced by the facility in one year on a reasonable basis other than by reference to nameplate capacity, such as the average expected annual output of the facility.

Commentators suggested that the 20 percent threshold be increased to 30 percent in order to be consistent with longstanding IRS ruling positions that pre-dated the issuance of regulations under section 141 for output facilities (*e.g.*, Rev. Proc. 89–3, 1989–1 C.B. 761). The final regulations adopt this comment and change the 20 percent threshold to 30 percent.

8. *Special exception for sales of output attributable to excess generating capacity resulting from open access*

The temporary regulations contain an exception to private business use for certain purchases of output of an electric generating facility if: (1) the contract term does not exceed three years; (2) the issuer does not utilize tax-exempt financing to increase the generating capacity of its system by more than three percent during the contract term; (3) the governmental owner offers certain non-discriminatory, open access transmission tariffs; (4) all of the output sold is attributable to excess capacity resulting from the offer of the open access tariffs; and (5) all payments received by the governmental owner under the contract (other than the portion allocable to operation and maintenance expenses described in § 1.141–4(c)(2)(C)) are applied as promptly as is reasonably practical to redeem tax-exempt bonds in a manner consistent with § 1.141–12.

Some commentators stated that this exception contains overly restrictive requirements that significantly limit its usefulness. These commentators recommended that the exception be expanded to apply to: (1) sales in anticipation of open access or retail competition; (2) sales to native load customers if open access is in effect or reasonably expected to commence within a reasonable time period; and (3) contracts with terms in excess of three years. These commentators also requested clarification regarding the requirement to redeem bonds, the extent to which the rules in § 1.141–12 apply, and the limitations on tax-exempt financing during the contract term.

These suggested changes raise a number of administrability issues. For example, in many cases it may be difficult to predict the nature and extent of an issuer's future participation in open access or to determine whether a particular sale is made in anticipation of open access. In light of these administrability concerns and the expansion of the short-term contract exception to three years as described above, the final regulations delete the special exception for excess capacity-related sales.

9. *Special rules for electric output facilities used to provide open access*

Under the temporary regulations, the use of electric generation, transmission or distribution facilities by a nongovernmental person may result in private business use under the benefits and burdens test. In addition, the use of electric facilities under arrangements other than output contracts may constitute private business use under the general rules of § 1.141–3.

The temporary regulations do not contain specific provisions for determining whether the use of electric output facilities by a regional transmission organization (RTO), independent system operator (ISO) or other independent transmission operator results in private business use. However, the preamble to the temporary regulations states that the rules for management contracts under section 141, including Revenue Procedure 97–13, 1997–1 C.B. 632, apply in this regard.

Commentators stated that the management contract guidelines in Revenue Procedure 97–13 are not well-tailored to address the use of electric facilities by an RTO or an ISO. They requested additional guidance concerning the circumstances in which an RTO or an ISO will not be treated as a private business user. The final regulations provide that a contract for the operation of an electric transmission facility by an independent entity, such as an RTO or an ISO (*independent transmission operator*), does not result in private business use of the facility if: (1) the facility is owned by a governmental person; (2) the operation of the facility by the independent transmission operator is approved by the Federal Energy Regulatory Commission (FERC) under provisions of the Federal Power Act (16 U.S.C. 791a through 825r) (or by a state authority under comparable provisions of state law); (3) the independent transmission operator's compensation is not based on a share of net profits from the facility; and (4) the independent transmission operator does not bear risk of loss of the facility.

The temporary regulations contain two special exceptions under which certain actions involving electric transmission or distribution facilities are not treated as deliberate actions under § 1.141–2(d). The first exception applies to certain contracts entered into in response to, or in anticipation of, an order by the FERC to wheel power under the Federal Power Act, or by a state authority under comparable state law. The second exception applies to certain actions to implement the offering of non-discriminatory, open access tariffs in a manner consistent with certain FERC rules under the Federal Power Act or comparable state law. The final regulations retain these special exceptions.

Commentators requested additional guidance regarding the circumstances in which electric transmission and distribution facilities that are available for use on a non-discriminatory, open access basis will not be used for a private business use. The final regulations provide that the use of an electric transmission or distribution facility by a nongovernmental person pursuant to an output contract does not result in private business use if: (1) the facility is owned by a governmental person; (2) the facility is available for use on a nondiscriminatory, open access basis (a transmission facility meets this requirement if it is operated by a qualifying independent transmission operator); and (3) the facility is not financed for a principal purpose of serving that nongovernmental person.

B. *§ 1.141–8 $15 Million Limitation for Output Facilities*

The temporary regulations provide guidance on the special $15 million limitation on output facilities of section 141(b)(4). In general, this limitation is based on the nonqualified amount of an issue or issues that finance a single project.

The temporary regulations provide that facilities having different purposes or serving different customer bases are not ordinarily part of the same project. For example, a peaking unit and a baseload unit generally are not part of the same project.

The temporary regulations also provide that, in the case of generation and related facilities, project means property located at the same site. However, separate generating units are not part of the same project if one unit is reasonably expected, on the issue date of each issue that finances the facilities, to be placed in service more than three years before the other.

Some commentators noted that there is an ambiguity in the temporary regulations regarding whether a peaking unit and a baseload unit that are located at the same site and placed in service within the same three-year period are part of the same project. The final regulations clarify that a peaking unit and a baseload unit generally are not part of the same project, even if they are located at the same site and placed in service within the same three-year period.

C. *Need for Final Regulations*

Congress passed the Energy Policy Act of 1992, Public Law 102–486 (106 Stat. 2776), to encourage restructuring of the electric power industry. Since that time, the FERC and many states have adopted policies to provide open access to transmission and distribution facilities. Treasury and the IRS are aware that these initiatives have caused many changes in the electric power industry, and that restructuring efforts are ongoing. The temporary regulations were published in order to provide immediate guidance under section 141 regarding the effect on the tax-exempt status of bonds of certain restructuring transactions necessary for utilities to participate in a restructured electric utility industry.

Commentators stated that the lack of final regulations addressing these issues has hindered public power systems in undertaking long-term planning. Commentators also stated that uncertainty regarding the characterization under the private business tests of certain open access transactions has hampered participation by public power systems in open access plans. The final regulations are being issued at this time in order to address these concerns, notwithstanding that restructuring initiatives continue to evolve. It is anticipated that the special rules in the final regulations for open access transactions will not result in a significant increase in the volume of tax-exempt bonds for output facilities. In the event that such an increase does occur, Treasury and the IRS may reconsider relevant aspects of the regulations and propose additional limitations on the use of tax-exempt financing for such facilities.

Effective Dates

The final regulations apply to bonds sold on or after November 22, 2002.

Special Analyses

It has been determined that this Treasury decision is not a significant regulatory action as defined in Executive Order 12866. Therefore, a regulatory assessment is not required. It has also been determined that section 553(b) of the Administrative Procedure Act (5 U.S.C. chapter 5) does not apply to these regulations, and because the rule does not impose a collection of information on small entities, the provisions of the Regulatory Flexibility Act (5 U.S.C. 601 *et seq.*) do not apply.

Drafting Information

The principal authors of these regulations are Bruce M. Serchuk and Rose M. Weber, Office of Chief Counsel (Tax Exempt and Government Entities), Internal Revenue Service, and Stephen J. Watson, Office of Tax Legislative Counsel, Department of the Treasury. However, other personnel from the IRS and Treasury Department participated in their development.

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Adoption of Amendments to the Regulations

Accordingly, 26 CFR part 1 is amended as follows:

PART 1—INCOME TAXES

Paragraph 1. The authority citation for part 1 continues to read in part as follows:

Authority: 26 U.S.C. 7805 * * *

Par. 2. Section 1.141–0 is amended by removing the entries for §§ 1.141–7T, 1.141–8T and 1.141–15T and adding entries to the table in numerical order for §§ 1.141–7, 1.141–8 and 1.141–15(f) through (i) to read as follows:

§ 1.141–0 Table of contents.

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§ 1.141–7 Special rules for output facilities.

§ 1.141–8 $15 million limitation for output facilities.

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§ 1.141–15 Effective dates.

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(g) Refunding bonds for output facilities.
(h) Permissive retroactive application.
(i) Permissive application of certain regulations relating to output facilities.

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Par. 3. Section 1.141–2 is amended by revising the last sentence of paragraph (d)(3)(ii)(B) to read as follows:

§ 1.141–2 Private activity bond tests.

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(d) * * *
(3) * * *
(ii) * * *
(B) * * * See § 1.141–7(g)(4).

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Par. 4. Section 1.141–7 is added to read as follows:

§ 1.141–7 Special rules for output facilities.

(a) *Overview.* This section provides special rules to determine whether arrangements for the purchase of output from an output facility cause an issue of bonds to meet the private business tests. For this purpose, unless otherwise stated, water facilities are treated as output facilities. Sections 1.141–3 and 1.141–4 generally apply to determine whether other types of arrangements for use of an output facility cause an issue to meet the private business tests.

(b) *Definitions.* For purposes of this section and § 1.141–8, the following definitions and rules apply:

(1) *Available output.* The available output of a facility financed by an issue is determined by multiplying the number of units produced or to be produced by the facility in one year by the number of years in the measurement period of that facility for that issue.

(i) *Generating facilities.* The number of units produced or to be produced by a generating facility in one year is determined by reference to its nameplate capacity or the equivalent (or where there is no nameplate capacity or the equivalent, its maximum capacity), which is not reduced for reserves, maintenance or other unutilized capacity.

(ii) *Transmission and other output facilities*—(A) *In general*. For transmission, distribution, cogeneration, and other output facilities, available output must be measured in a reasonable manner to reflect capacity.

(B) *Electric transmission facilities.* Measurement of the available output of all or a portion of electric transmission facilities may be determined in a manner consistent with the reporting rules and requirements for transmission networks promulgated by the Federal Energy Regulatory Commission (FERC). For example, for a transmission network, the use of aggregate load and load share ratios in a manner consistent with the requirements of the FERC may be reasonable. In addition, depending on the facts and circumstances, measurement of the available output of transmission facilities using thermal capacity or transfer capacity may be reasonable.

(iii) *Special rule for facilities with significant unutilized capacity.* If an issuer reasonably expects on the issue date that persons that are treated as private business users will purchase more than 30 percent of the actual output of the facility financed with the issue, the Commissioner may determine the number of units produced or to be produced by the facility in one year on a reasonable basis other than by reference to nameplate or other capacity, such as the average expected annual output of the facility. For example, the Commissioner may determine the available output of a financed peaking electric generating unit by reference to the reasonably expected annual output of that unit if the issuer reasonably expects, on the issue date of bonds that finance the unit, that an investor-owned utility will purchase more than 30 percent of the actual output of the facility during the measurement period under a take or pay contract, even if the amount of output purchased is less than 10 percent of the available output determined by reference to nameplate capacity. The reasonably expected annual output of the generating facility must be consistent with the capacity reported for prudent reliability purposes.

(iv) *Special rule for facilities with a limited source of supply.* If a limited source of supply constrains the output of an output facility, the number of units produced or to be produced by the facility must be determined by reasonably taking into account those constraints. For this purpose, a limited source of supply shall include a physical limitation (for example, flow of water), but not an economic limitation (for example, cost of coal or gas). For example, the available output of a hydroelectric unit must be determined by reference to the reasonably expected annual flow of water through the unit.

(2) *Measurement period.* The measurement period of an output facility financed by an issue is determined under § 1.141–3(g).

(3) *Sale at wholesale.* A sale at wholesale means a sale of output to any person for resale.

(4) *Take contract and take or pay contract.* A *take contract* is an output contract under which a purchaser agrees to pay for the output under the contract if the output facility is capable of providing the output. A *take or pay contract* is an output contract under which a purchaser agrees to pay for the output under the contract, whether or not the output facility is capable of providing the output.

(5) *Requirements contract*. A *requirements contract* is an output contract, other than a take contract or a take or pay contract, under which a nongovernmental person agrees to purchase all or part of its output requirements.

(6) *Nonqualified amount.* The nonqualified amount with respect to an issue is determined under section 141(b)(8).

(c) *Output contracts*—(1) *General rule*. The purchase pursuant to a contract by a nongovernmental person of available output of an output facility (output contract) financed with proceeds of an issue is taken into account under the private business tests if the purchase has the effect of transferring the benefits of owning the facility and the burdens of paying the debt service on bonds used (directly or indirectly) to finance the facility (the benefits and burdens test). See paragraph (c)(4) of this section for the treatment of an output contract that is properly characterized as a lease for Federal income tax purposes. See paragraphs (d) and (e) of this section for rules regarding measuring the use of, and payments of debt service for, an output facility for determining whether the private business tests are met. See also § 1.141–8 for rules for when an issue that finances an output facility (other than a water facility) meets the private business tests because the nonqualified amount of the issue exceeds $15 million.

(2) *Take contract or take or pay contract.* The benefits and burdens test is met if a nongovernmental person agrees pur-

suant to a take contract or a take or pay contract to purchase available output of a facility.

(3) *Requirements contract*—(i) *In general*. A requirements contract may satisfy the benefits and burdens test under paragraph (c)(3)(ii) or (iii) of this section. See § 1.141–15(f)(2) for special effective dates for the application of this paragraph (c)(3) to issues financing facilities subject to requirements contracts.

(ii) *Requirements contract similar to take contract or take or pay contract.* A requirements contract generally meets the benefits and burdens test to the extent that it contains contractual terms that obligate the purchaser to make payments that are not contingent on the output requirements of the purchaser or that obligate the purchaser to have output requirements. For example, a requirements contract with an industrial purchaser meets the benefits and burdens test if the purchaser enters into additional contractual obligations with the issuer or another governmental unit not to cease operations. A requirements contract does not meet the benefits and burdens test, however, by reason of a provision that requires the purchaser to pay reasonable and customary damages (including liquidated damages) in the event of a default, or a provision that permits the purchaser to pay a specified amount to terminate the contract while the purchaser has requirements, in each case if the amount of the payment is reasonably related to the purchaser's obligation to buy requirements that is discharged by the payment.

(iii) *Wholesale requirements contract*—(A) *In general.* A requirements contract that is a sale at wholesale (a *wholesale requirements contract*) may satisfy the benefits and burdens test, depending on all the facts and circumstances.

(B) *Significant factors.* Significant factors that tend to establish that a wholesale requirements contract meets the benefits and burdens test include, but are not limited to—

(1) The term of the contract is substantial relative to the term of the issue or issues that finance the facility; and

(2) The amount of output to be purchased under the contract represents a substantial portion of the available output of the facility.

(C) *Safe harbors.* A wholesale requirements contract does not meet the benefits and burdens test if—

(1) The term of the contract, including all renewal options, does not exceed the lesser of 5 years or 30 percent of the term of the issue; or

(2) The amount of output to be purchased under the contract (and any other requirements contract with the same purchaser or a related party with respect to the facility) does not exceed 5 percent of the available output of the facility.

(iv) *Retail requirements contract.* Except as otherwise provided in this paragraph (c)(3), a requirements contract that is not a sale at wholesale does not meet the benefits and burdens test.

(4) *Output contract properly characterized as a lease*. Notwithstanding any other provision of this section, an output contract that is properly characterized as a lease for Federal income tax purposes shall be tested under the rules contained in §§ 1.141–3 and 1.141–4 to determine whether it is taken into account under the private business tests.

(d) *Measurement of private business use.* If an output contract results in private business use under this section, the amount of private business use generally is the amount of output purchased under the contract.

(e) *Measurement of private security or payment.* The measurement of payments made or to be made by nongovernmental persons under output contracts as a percent of the debt service of an issue is determined under the rules provided in § 1.141–4.

(f) *Exceptions for certain contracts*—(1) *Small purchases of output.* An output contract for the use of a facility is not taken into account under the private business tests if the average annual payments to be made under the contract do not exceed 1 percent of the average annual debt service on all outstanding tax-exempt bonds issued to finance the facility, determined as of the effective date of the contract.

(2) *Swapping and pooling arrangements.* An agreement that provides for swapping or pooling of output by one or more governmental persons and one or more nongovernmental persons does not result in private business use of the output facility owned by the governmental person to the extent that—

(i) The swapped output is reasonably expected to be approximately equal in value (determined over periods of three years or less); and

(ii) The purpose of the agreement is to enable each of the parties to satisfy different peak load demands, to accommodate temporary outages, to diversify supply, or to enhance reliability in accordance with prudent reliability standards.

(3) *Short-term output contracts.* An output contract with a nongovernmental person is not taken into account under the private business tests if—

(i) The term of the contract, including all renewal options, is not longer than 3 years;

(ii) The contract either is a negotiated, arm's-length arrangement that provides for compensation at fair market value, or is based on generally applicable and uniformly applied rates; and

(iii) The output facility is not financed for a principal purpose of providing that facility for use by that nongovernmental person.

(4) *Certain conduit parties disregarded.* A nongovernmental person acting solely as a conduit for the exchange of output among governmentally owned and operated utilities is disregarded in determining whether the private business tests are met with respect to financed facilities owned by a governmental person.

(g) *Special rules for electric output facilities used to provide open access*—(1) *Operation of transmission facilities by nongovernmental persons*—(i) *In general.* The operation of an electric transmission facility by a nongovernmental person may result in private business use of the facility under § 1.141–3 and this section based on all the facts and circumstances. For example, a transmission facility is generally used for a private business use if a nongovernmental person enters into a contract to operate the facility and receives compensation based, in whole or in part, on a share of net profits from the operation of the facility.

(ii) *Certain use by independent transmission operators.* A contract for the operation of an electric transmission facility by an independent entity, such as a regional transmission organization or an independent system operator (*independent transmission operator*), does not constitute private business use of the facility if—

(A) The facility is owned by a governmental person;

(B) The operation of the facility by the independent transmission operator is approved by the FERC under one or more provisions of the Federal Power Act (16 U.S.C. 791a through 825r) (or by a state authority under comparable provisions of state law);

(C) No portion of the compensation of the independent transmission operator is based on a share of net profits from the operation of the facility; and

(D) The independent transmission operator does not bear risk of loss of the facility.

(2) *Certain use by nongovernmental persons under output contracts*—(i) *Transmission facilities*. The use of an electric transmission facility by a nongovernmental person pursuant to an output contract does not constitute private business use of the facility if—

(A) The facility is owned by a governmental person;

(B) The facility is operated by an independent transmission operator in a manner that satisfies paragraph (g)(1)(ii) of this section; and

(C) The facility is not financed for a principal purpose of providing that facility for use by that nongovernmental person.

(ii) *Distribution facilities.* The use of an electric distribution facility by a nongovernmental person pursuant to an output contract does not constitute private business use of the facility if—

(A) The facility is owned by a governmental person;

(B) The facility is available for use on a nondiscriminatory, open access basis by buyers and sellers of electricity in accordance with rates that are generally applicable and uniformly applied within the meaning of § 1.141–3(c)(2); and

(C) The facility is not financed for a principal purpose of providing that facility for use by that nongovernmental person (other than a retail end-user).

(3) *Ancillary services*. The use of an electric output facility to provide ancillary services required to be offered as part of an open access transmission tariff under rules promulgated by the FERC under the Federal Power Act (16 U.S.C. 791a through 825r) does not result in private business use.

(4) *Exceptions to deliberate action rules*—(i) *Mandated wheeling.* Entering into a contract for the use of electric transmission or distribution facilities is not treated as a deliberate action under § 1.141–2(d) if—

(A) The contract is entered into in response to (or in anticipation of) an order by the United States under sections 211 and 212 of the Federal Power Act (16 U.S.C. 824j and 824k) (or a state regulatory authority under comparable provisions of state law); and

(B) The terms of the contract are *bona fide* and arm's-length, and the consideration paid is consistent with the provisions of section 212(a) of the Federal Power Act.

(ii) *Actions taken to implement nondiscriminatory, open access*. An action is not treated as a deliberate action under § 1.141–2(d) if it is taken to implement the offering of non-discriminatory, open access tariffs for the use of electric transmission or distribution facilities in a manner consistent with rules promulgated by the FERC under sections 205 and 206 of the Federal Power Act (16 U.S.C. 824d and 824e) (or comparable provisions of state law). This paragraph (g)(4)(ii) does not apply, however, to the sale, exchange, or other disposition (within the meaning of section 1001(a)) of transmission or distribution facilities to a nongovernmental person.

(iii) *Application of reasonable expectations test to certain current refunding bonds.* An action taken or to be taken with respect to electric transmission or distribution facilities refinanced by an issue is not taken into account under the reasonable expectations test of § 1.141–2(d) if—

(A) The action is described in paragraph (g)(4)(i) or (ii) of this section;

(B) The bonds of the issue are current refunding bonds that refund bonds originally issued before February 23, 1998; and

(C) The weighted average maturity of the refunding bonds is not greater than the remaining weighted average maturity of the prior bonds.

(5) *Additional transactions as permitted by the Commissioner.* The Commissioner may, by published guidance, set forth additional circumstances in which the use of electric output facilities in a restructured electric industry does not constitute private business use.

(h) *Allocations of output facilities and systems*—(1) *Facts and circumstances analysis.* Whether output sold under an output contract is allocated to a particular facility (for example, a generating unit), to the entire system of the seller of that output (net of any uses of that system output allocated to a particular facility), or to a portion of a facility is based on all the facts and circumstances. Significant factors to be considered in determining the allocation of an output contract to financed property are the following:

(i) The extent to which it is physically possible to deliver output to or from a particular facility or system.

(ii) The terms of a contract relating to the delivery of output (such as delivery limitations and options or obligations to deliver power from additional sources).

(iii) Whether a contract is entered into as part of a common plan of financing for a facility.

(iv) The method of pricing output under the contract, such as the use of market rates rather than rates designed to pay debt service of tax-exempt bonds used to finance a particular facility.

(2) *Illustrations*. The following illustrate the factors set forth in paragraph (h)(1) of this section:

(i) *Physical possibility*. Output from a generating unit that is fed directly into a low voltage distribution system of the owner of that unit and that cannot physically leave that distribution system generally must be allocated to those receiving electricity through that distribution system. Output may be allocated without regard to physical limitations, however, if exchange or similar agreements provide output to a purchaser where, but for the exchange agreements, it would not be possible for the seller to provide output to that purchaser.

(ii) *Contract terms relating to performance*. A contract to provide a specified amount of electricity from a system, but only when at least that amount of electricity is being generated by a particular unit, is allocated to that unit. For example, a contract to buy 20 MW of system power with a right to take up to 40 percent of the actual output of a specific 50 MW facility whenever total system output is insufficient to meet all of the seller's obligations generally is allocated to the specific facility rather than to the system.

(iii) *Common plan of financing*. A contract entered into as part of a common plan of financing for a facility generally is allocated to the facility if debt service for the issue of bonds is reasonably expected to be paid, directly or indirectly, from payments under the contract.

(iv) *Pricing method*. Pricing based on the capital and generating costs of a particular turbine tends to indicate that output under the contract is properly allocated to that turbine.

(3) *Transmission and distribution contracts*. Whether use under an output contract for transmission or distribution is allocated to a particular facility or to a transmission or distribution network is based on all the facts and circumstances, in a manner similar to paragraphs (h)(1) and (2) of this section. In general, the method used to determine payments under a contract is a more significant contract term for this purpose than nominal contract path. In general, if reasonable and consistently applied, the determination of use of transmission or distribution facilities under an output contract may be based on a method used by third parties, such as reliability councils.

(4) *Allocation of payments*. Payments for output provided by an output facility financed with two or more sources of funding are generally allocated under the rules in § 1.141–4(c).

(i) *Examples*. The following examples illustrate the application of this section:

Example 1. Joint ownership. Z, an investor-owned electric utility, and City H agree to construct an electric generating facility of a size sufficient to take advantage of the economies of scale. H will issue $50 million of its 24-year bonds, and Z will use $100 million of its funds for construction of a facility they will jointly own as tenants in common. Each of the participants will share in the ownership, output, and operating expenses of the facility in proportion to its contribution to the cost of the facility, that is, one-third by H and two-thirds by Z. H's bonds will be secured by H's ownership interest in the facility and by revenues to be derived from its share of the annual output of the facility. H will need only 50 percent of its share of the annual output of the facility during the first 20 years of operations. It agrees to sell 10 percent of its share of the annual output to Z for a period of 20 years pursuant to a contract under which Z agrees to take that power if available. The facility will begin operation, and Z will begin to receive power, 4 years after the H bonds are issued. The measurement period for the property financed by the issue is 20 years. H also will sell the remaining 40 percent of its share of the annual output to numerous other private utilities under contracts of three years or less that satisfy the exception under paragraph (f)(3) of this section. No other contracts will be executed obligating any person to purchase any specified amount of the power for any specified period of time. No person (other than Z) will make payments that will result in a transfer of the burdens of paying debt service on bonds used directly or indirectly to provide H's share of the facilities. The bonds are not private activity bonds, because H's one-third interest in the facility is not treated as used by the other owners of the facility. Although 10 percent of H's share of the annual output of the facility will be used in the trade or business of Z, a nongovernmental person, under this section, that portion constitutes not more than 10 percent of the available output of H's ownership interest in the facility.

Example 2. Wholesale requirements contract. (i) City J issues 20-year bonds to acquire an electric generating facility having a reasonably expected economic life substantially greater than 20 years and a nameplate capacity of 100 MW. The available output of the facility under paragraph (b)(1) of this section is approximately 17,520,000 MWh (100 MW X 24 hours X 365 days X 20 years). On the issue date, J enters into a contract with T, an investor-owned utility, to provide T with all of its power requirements for a period of 10 years, commencing on the issue date. J reasonably expects that T will actually purchase an average of 30 MW over the 10-year period. The contract is taken into account under the private business tests pursuant to paragraph (c)(3) of this section because the term of the contract is substantial relative to the term of the issue and the amount of output to be purchased is a substantial portion of the available output.

(ii) Under paragraph (d) of this section, the amount of reasonably expected private business use under this contract is approximately 15 percent (30 MW X 24 hours X 365 days X 10 years, or 2,628,000 MWh) of the available output. Accordingly, the issue meets the private business use test. J reasonably expects that the amount to be paid for an average of 30 MW of power (less the operation and maintenance costs directly attributable to generating that 30 MW of power), will be more than 10 percent of debt service on the issue on a present-value basis. Accordingly, the issue meets the private security or payment test because J reasonably expects that payment of more than 10 percent of the debt service will be indirectly derived from payments by T. The bonds are private activity bonds under paragraph (c) of this section. Further, if 15 percent of the sale proceeds of the issue is greater than $15 million and the issue meets the private security or payment test with respect to the $15 million output limitation, the bonds are also private activity bonds under section 141(b)(4). See § 1.141–8.

Example 3. Retail contracts. (i) State Agency M, a political subdivision, issues bonds in 2003 to finance the construction of a generating facility that will be used to furnish electricity to M's retail customers. In 2007, M enters into a 10-year contract with industrial corporation I. Under the contract, M agrees to supply I with all of its power requirements during the contract term, and I agrees to pay for that power at a negotiated price as it is delivered. The contract does not require I to pay for any power except to the extent I has requirements. In addition, the contract requires I to pay reasonable and customary liquidated damages in the event of a default by I, and permits I to terminate the contract while it has requirements by paying M a specified amount that is a reasonable and customary amount for terminating the contract. Any damages or termination payment by I will be reasonably related to I's obligation to buy requirements that is discharged by the payment. Under paragraph (c)(3) of this section, the contract does not meet the benefits and burdens test. Thus, it is not taken into account under the private business tests.

(ii) The facts are the same as in paragraph (i) of this *Example 3*, except that the contract requires I to make guaranteed minimum payments, regardless of I's requirements, in an amount such that the contract does not meet the exception for small purchases in paragraph (f)(1) of this section. Under paragraph (c)(3)(ii) of this section, the contract meets the benefits and burdens test because it obligates I to make payments that are not contingent on its output requirements. Thus, it is taken into account under the private business tests.

Example 4. Allocation of existing contracts to new facilities. Power Authority K, a political subdivision created by the legislature in State X to own and operate certain power generating facilities, sells all of the power from its existing facilities to four private utility systems under contracts executed in 1999, under which the four systems are required to take or pay for specified portions of the total power output until the year 2029. Existing facilities supply all of the present needs of the four utility systems, but their future power requirements are expected to increase substantially beyond the capacity of K's current generating system. K issues 20-year bonds in 2004 to construct a large generating facility. As part of the financing plan for the bonds, a fifth private utility system contracts with K to take or pay for 15 percent of the available output of the new facility. The balance of the output of the new facility will be available for sale as required, but initially it is not anticipated that there will be any need for that power. The revenues from the contract with the fifth private utility system will be sufficient to pay less than 10 percent of the debt service on the bonds (determined on a present value basis). The balance, which will exceed 10 percent of the debt service on the bonds, will be paid from revenues derived from the contracts with the four systems initially from sale of power produced by the old facilities. The output contracts with all the private utilities are allocated to K's entire generating system. See paragraphs (h)(1) and (2) of this section. Thus, the bonds meet the private business use test because more than 10 percent of the proceeds will be used in the trade or business of a nongovernmental person. In addition, the bonds meet the private security or payment test because payment of more than 10 percent of the debt service, pursuant to underlying arrangements, will be derived from payments in respect of property used for a private business use.

Example 5. Allocation to displaced resource. Municipal utility MU, a political subdivision, purchases all of the electricity required to meet the needs of its customers (1,000 MW) from B, an investor-owned utility that operates its own electric generating facilities, under a 50-year take or pay contract. MU does not anticipate that it will require additional electric resources, and any new resources would produce electricity at a higher cost to MU than its cost under its contract with B. Nevertheless, B encourages MU to construct a new generating plant sufficient to meet MU's requirements. MU issues obligations to construct facilities that will produce 1,000 MW of electricity. MU, B, and I, another investor-owned utility, enter into an agreement under which MU assigns to I its rights under MU's take or pay contract with B.

Under this arrangement, I will pay MU, and MU will continue to pay B, for the 1,000 MW. I's payments to MU will at least equal the amounts required to pay debt service on MU's bonds. In addition, under paragraph (h)(1)(iii) of this section, the contract among MU, B, and I is entered into as part of a common plan of financing of the MU facilities. Under all the facts and circumstances, MU's assignment to I of its rights under the original take or pay contract is allocable to MU's new facilities under paragraph (h) of this section. Because I is a nongovernmental person, MU's bonds are private activity bonds.

Example 6. Operation of transmission facilities by regional transmission organization. (i) Public Power Agency D is a political subdivision that owns and operates electric generation, transmission and distribution facilities. In 2003, D transfers operating control of its transmission system to a regional transmission organization (RTO), a nongovernmental person, pursuant to an operating agreement that is approved by the FERC under sections 205 and 206 of the Federal Power Act. D retains ownership of its facilities. No portion of the RTO's compensation is based on a share of net profits from the operation of D's facilities, and the RTO does not bear any risk of loss of those facilities. Under paragraph (g)(1)(ii) of this section, the RTO's use of D's facilities does not constitute a private business use.

(ii) Company A is located in D's service territory. In 2004, Power Supplier E, a nongovernmental person, enters into a 10-year contract with A to supply A's electricity requirements. The electricity supplied by E to A will be transmitted over D's transmission and distribution facilities. D's distribution facilities are available for use on a nondiscriminatory, open access basis by buyers and sellers of electricity in accordance with rates that are generally applicable and uniformly applied within the meaning of § 1.141–3(c)(2). D's facilities are not financed for a principal purpose of providing the facilities for use by E. Under paragraph (g)(2) of this section, the contract between A and E does not result in private business use of D's facilities.

Example 7. Certain actions not treated as deliberate actions. The facts are the same as in *Example 6* of this paragraph (i), except that the RTO's compensation is based on a share of net profits from operating D's facilities. In addition, D had issued bonds in 1994 to finance improvements to its transmission system. At the time D transfers operating control of its transmission system to the RTO, D chooses to apply the private activity bond regulations of §§ 1.141–1 through 1.141–15 to the 1994 bonds. The operation of D's facilities by the RTO results in private business use under § 1.141–3 and paragraph (g)(1)(i) of this section. Under the special exception in paragraph (g)(4)(ii) of this section, however, the transfer of control is not treated as a deliberate action. Accordingly, the transfer of control does not cause the 1994 bonds to meet the private activity bond tests.

Example 8. Current refunding. The facts are the same as in *Example 7* of this paragraph (i), and in addition D issues bonds in 2004 to currently refund the 1994 bonds. The weighted average maturity of the 2004 bonds is not greater than the remaining weighted average maturity of the 1994 bonds. D chooses to apply the private activity bond regulations of §§ 1.141–1 through 1.141–15 to the refunding bonds. In general, reasonable expectations must be separately tested on the date that refunding bonds are issued under § 1.141–2(d). Under the special exception in paragraph (g)(4)(iii) of this section, however, the transfer of the financed facilities to the RTO need not be taken into account in applying the reasonable expectations test to the refunding bonds.

§ 1.141–7T [Removed]

Par. 5. Section 1.141–7T is removed.

Par. 6. Section 1.141–8 is added to read as follows:

§ 1.141–8 $15 million limitation for output facilities.

(a) *In general*—(1) *General rule*. Section 141(b)(4) provides a special private activity bond limitation (the $15 million output limitation) for issues 5 percent or more of the proceeds of which are to be used to finance output facilities (other than a facility for the furnishing of water). Under this rule, an issue consists of private activity bonds under the private business tests of section 141(b)(1) and (2) if the nonqualified amount with respect to output facilities financed by the proceeds of the issue exceeds $15 million. The $15 million output limitation applies in addition to the private business tests of section 141(b)(1) and (2). Under section 141(b)(4) and paragraph (a)(2) of this section, the $15 million output limitation is reduced in certain cases. Specifically, an issue meets the test in section 141(b)(4) if both of the following tests are met:

(i) More than $15 million of the proceeds of the issue to be used with respect to an output facility are to be used for a private business use. Investment proceeds are disregarded for this purpose if they are not allocated disproportionately to the private business use portion of the issue.

(ii) The payment of the principal of, or the interest on, more than $15 million of the sale proceeds of the portion of the issue used with respect to an output facility is (under the terms of the issue or any underlying arrangement) directly or indirectly—

(A) Secured by any interest in an output facility used or to be used for a private business use (or payments in respect of such an output facility); or

(B) To be derived from payments (whether or not to the issuer) in respect of an output facility used or to be used for a private business use.

(2) *Reduction in $15 million output limitation for outstanding issues*—(i) *General rule*. In determining whether an issue 5 percent or more of the proceeds of which are to be used with respect to an output facility consists of private activity bonds under the $15 million output limitation, the $15 million limitation on private business use and private security or payments is applied by taking into account the aggregate nonqualified amounts of any outstanding bonds of other issues 5 percent or more of the proceeds of which are or will be used with respect to that output facility or any other output facility that is part of the same project.

(ii) *Bonds taken into account*. For purposes of this paragraph (a)(2), in applying the $15 million output limitation to an issue (the later issue), a tax-exempt bond of another issue (the earlier issue) is taken into account if—

(A) That bond is outstanding on the issue date of the later issue;

(B) That bond will not be redeemed within 90 days of the issue date of the later issue in connection with the refunding of that bond by the later issue; and

(C) 5 percent or more of the sale proceeds of the earlier issue financed an output facility that is part of the same project as the output facility that is financed by 5 percent or more of the sale proceeds of the later issue.

(3) *Benefits and burdens test applicable*—(i) *In general*. In applying the $15 million output limitation, the benefits and burdens test of § 1.141–7 applies, except that "$15 million" is applied in place of "10 percent", or "5 percent" as appropriate.

(ii) *Earlier issues for the project*. If bonds of an earlier issue are outstanding and must be taken into account under paragraph (a)(2) of this section, the nonqualified amount for that earlier issue is multiplied by a fraction, the numerator of which is the adjusted issue price of the earlier issue as of the issue date of the later issue, and the denominator of which is the issue price of the earlier issue. Pre-issuance accrued interest as defined in § 1.148–1(b) is disregarded for this purpose.

(b) *Definition of project*—(1) *General rule*. For purposes of paragraph (a)(2) of this section, *project* has the meaning provided in this paragraph. Facilities that are functionally related and subordinate to a project are treated as part of that same project. Facilities having different purposes or serving different customer bases are not ordinarily part of the same project. For example, the following are generally not part of the same project—

(i) Generation, transmission and distribution facilities;

(ii) Separate facilities designed to serve wholesale customers and retail customers; and

(iii) A peaking unit and a baseload unit (regardless of the location of the units).

(2) *Separate ownership.* Except as otherwise provided in this paragraph (b)(2), facilities that are not owned by the same person are not part of the same project. If different governmental persons act in concert to finance a project, however (for example as participants in a joint powers authority), their interests are aggregated with respect to that project to determine whether the $15 million output limitation is met. In the case of undivided ownership interests in a single output facility, property that is not owned by different persons is treated as separate projects only if the separate interests are financed—

(i) With bonds of different issuers; and

(ii) Without a principal purpose of avoiding the limitation in this section.

(3) *Generating property*—(i) *Property on same site.* In the case of generation and related facilities, *project* means property located at the same site.

(ii) *Special rule for generating units.* Separate generating units are not part of the same project if one unit is reasonably expected, on the issue date of each issue that finances the units, to be placed in service more than 3 years before the other. Common facilities or property that will be functionally related to more than one generating unit must be allocated on a reasonable basis. If a generating unit already is constructed or is under construction (the first unit) and bonds are to be issued to finance an additional generating unit (the second unit), all costs for any common facilities paid or incurred before the earlier of the issue date of bonds to finance the second unit or the commencement of construction of the second unit are allocated to the first unit. At the time that bonds are issued to finance the second unit (or, if earlier, upon commencement of construction of that unit), any remaining costs of the common facilities may be allocated between the first and second units so that in the aggregate the allocation is reasonable.

(4) *Transmission and distribution.* In the case of transmission or distribution facilities, *project* means functionally related or contiguous property. Separate transmission or distribution facilities are not part of the same project if one facility is reasonably expected, on the issue date of each issue that finances the facilities, to be placed in service more than 2 years before the other.

(5) *Subsequent improvements*—(i) *In general.* An improvement to generation, transmission or distribution facilities that is not part of the original design of those facilities (the original project) is not part of the same project as the original project if the construction, reconstruction, or acquisition of that improvement commences more than 3 years after the original project was placed in service and the bonds issued to finance that improvement are issued more than 3 years after the original project was placed in service.

(ii) *Special rule for transmission and distribution facilities.* An improvement to transmission or distribution facilities that is not part of the original design of that property is not part of the same project as the original project if the issuer did not reasonably expect the need to make that improvement when it commenced construction of the original project and the construction, reconstruction, or acquisition of that improvement is mandated by the federal government or a state regulatory authority to accommodate requests for wheeling.

(6) *Replacement property*. For purposes of this section, property that replaces existing property of an output facility is treated as part of the same project as the replaced property unless—

(i) The need to replace the property was not reasonably expected on the issue date or the need to replace the property occurred more than 3 years before the issuer reasonably expected (determined on the issue date of the bonds financing the property) that it would need to replace the property; and

(ii) The bonds that finance (and refinance) the output facility have a weighted average maturity that is not greater than 120 percent of the reasonably expected economic life of the facility.

(c) *Example*. The application of the provisions of this section is illustrated by the following example:

Example. (i) Power Authority K, a political subdivision, intends to issue a single issue of tax-exempt bonds at par with a stated principal amount and sale proceeds of $500 million to finance the acquisition of an electric generating facility. No portion of the facility will be used for a private business use, except that L, an investor-owned utility, will purchase 10 percent of the output of the facility under a take contract and will pay 10 percent of the debt service on the bonds. The nonqualified amount with respect to the bonds is $50 million.

(ii) The maximum amount of tax-exempt bonds that may be issued for the acquisition of an interest in the facility in paragraph (i) of this *Example* is $465 million (that is, $450 million for the 90 percent of the facility that is governmentally owned and used plus a nonqualified amount of $15 million).

§ 1.141–8T [Removed]

Par. 7. Section 1.141–8T is removed.

Par. 8. Section 1.141–15 is amended by revising paragraph (a) and adding paragraphs (f), (g), (h) and (i) to read as follows:

§ 1.141–15 Effective dates.

(a) *Scope.* The effective dates of this section apply for purposes of §§ 1.141–1 through 1.141–6(a), 1.141–7 through 1.141–14, 1.145–1 through 1.145–2, 1.150–1(a)(3) and the definition of bond documents contained in § 1.150–1(b).

* * * * *

(f) *Effective dates for certain regulations relating to output facilities*—(1) *General rule.* Except as otherwise provided in this section, §§ 1.141–7 and 1.141–8 apply to bonds sold on or after November 22, 2002, that are subject to section 1301 of the Tax Reform Act of 1986 (100 Stat. 2602).

(2) *Transition rule for requirements contracts*. For bonds otherwise subject to §§ 1.141–7 and 1.141–8, § 1.141–7(c)(3) applies to output contracts entered into on or after September 19, 2002. An output contract is treated as entered into on or after that date if it is amended on or after that date, but only if the amendment results in a change in the parties to the contract or increases the amount of requirements covered by the contract by reason of an extension of the contract term or a change in the method for determining such requirements. For purposes of this paragraph (f)(2)—

(i) The extension of the term of a contract causes the contract to be treated as entered into on the first day of the additional term;

(ii) The exercise by a party of a legally enforceable right that was provided under a contract before September 19, 2002, on terms that were fixed and determinable before such date, is not treated as an amendment of the contract. For example, the exercise by a purchaser after September 19, 2002 of a renewal option that was provided under a contract before that date, on terms identical to the original contract, is not treated as an amendment of the contract; and

(iii) An amendment that increases the amount of requirements covered by the contract by reason of a change in the method for determining such requirements is treated as a separate contract that is entered into as of the effective date of the amendment, but only with respect to the increased output to be provided under the contract.

(g) *Refunding bonds for output facilities*. Except as otherwise provided in paragraph (h) or (i) of this section, §§ 1.141–7 and 1.141–8 do not apply to any bonds sold on or after November 22, 2002, to refund a bond to which §§ 1.141–7 and 1.141–8 do not apply unless—

(1) The refunding bonds are subject to section 1301 of the Tax Reform Act of 1986 (100 Stat. 2602); and

(2)(i) The weighted average maturity of the refunding bonds is longer than—

(A) The weighted average maturity of the refunded bonds; or

(B) In the case of a short-term obligation that the issuer reasonably expects to refund with a long-term financing (such as a bond anticipation note), 120 percent of the weighted average reasonably expected economic life of the facilities financed; or

(ii) A principal purpose for the issuance of the refunding bonds is to make one or more new conduit loans.

(h) *Permissive retroactive application.* Except as provided in paragraphs (d), (e) or (i) of this section, §§ 1.141–1 through 1.141–6(a), 1.141–7 through 1.141–14, 1.145–1 through 1.145–2, 1.150–1(a)(3) and the definition of bond documents contained in § 1.150–1(b) may be applied by issuers in whole, but not in part, to—

(1) Outstanding bonds that are sold before November 22, 2002, and subject to section 141; or

(2) Refunding bonds that are sold on or after November 22, 2002, and subject to section 141.

(i) *Permissive application of certain regulations relating to output facilities*. Issuers may apply §§ 1.141–7(f)(3) and 1.141–7(g) to any bonds.

§ 1.141–15T [Removed]

Par. 9. Section 1.141–15T is removed.

Robert E. Wenzel,
Deputy Commisionser
of Internal Revenue.

Approved September 17, 2002.

Pamela F. Olson,
Acting Assistant Secretary
of the Treasury.

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